1974 ANNUAL REPORT

EMCO

"Nineteen hundred and seventy-four was an outstanding year for your Company with the achievement of all-time record sales, earnings and return on shareholders' equity."

CONTENTS

ANNUAL MEETING

The Annual Meeting of the Shareholders of the Company will be held at Centennial Hall, 550 Wellington Street, in London at 11:00 A.M. on Thursday, May 22, 1975.

EMCO LIMITED

DIRECTORS

John W. Adams, F.C.A.
London, Ontario
Executive Vice-President
and Treasurer, Emco Limited

C. Norman Chapman
London, Ontario
President and
Chief Executive Officer
Emco Limited

W. Harold Evans
Toronto, Ontario
Retired Chairman
Honeywell Limited

Peter J. Ivey
London, Ontario
Vice-President
Pebojo Holdings Limited

Frederick W. P. Jones
London, Ontario
Business Consultant

Wayne B. Lyon
Taylor, Michigan
Executive Vice-President
Masco Corporation

Ralph S. MacLean
London, Ontario
Vice President
Plumbing and Industrial Group
Emco Limited

Richard A. Manoogian
Taylor, Michigan
Chairman of the Board, Emco Limited
President, Masco Corporation

Edwin C. Phillips
Vancouver, British Columbia
President
Westcoast Transmission Company Limited

Arman R. Simone
Detroit, Michigan
President
Simone Corporation

Robert W. Stevens, Q.C.
Toronto, Ontario
Partner
Blake, Cassels & Graydon

David B. Weldon
Toronto, Ontario
Chairman of the Board
Midland Doherty Limited

OFFICERS

Richard A. Manoogian
Chairman of the Board

C. Norman Chapman
President, Chief Executive Officer

John W. Adams, F.C.A.
Executive Vice-President and Treasurer

John G. Beresford
Vice-President, Engineered Products Group

Ralph S. MacLean
Vice-President, Plumbing and Industrial Group

Stuart F. Smith
Vice-President, General Manufacturing Division

A. Robert Martin, F.C.A.
Director, Corporate Development and Secretary

W. Wesley DeShane, C.A.
Comptroller and Assistant Secretary

TRANSFER AGENTS AND REGISTRARS

Royal Trust Company
Toronto, Montreal and Winnipeg
(5¾% debentures);
Toronto, Montreal, Winnipeg, Regina, Calgary and Vancouver
(7% convertible debentures, common shares and common share purchase warrants)
The Canada Trust Company
Toronto, Montreal and Winnipeg
(9¾% debentures)

AUDITORS

Peat, Marwick, Mitchell & Co.
London, Canada

To The Shareholders

FINANCIAL SUMMARY

Dollars in thousands except for shares

		1974	1973
Sales		$172,550	130,329
Earnings before extraordinary item		8,940	4,024
Extraordinary item		321	201
Net earnings	$	9,261	4,225
Per common share:			
Basic earnings:			
Before extraordinary item	$	2.00	1.07
Including extraordinary item		2.08	1.12
Fully diluted earnings:			
Before extraordinary item		1.91	.87
Including extraordinary item		1.97	.91
Capital expenditures	$	3,054	2,984


C. N. Chapman, President, Chief Executive Officer

Nineteen hundred and seventy-four was an outstanding year for your Company with the achievement of all-time record sales, earnings and return on shareholders' equity.

Sales for the year were $172.5 million, an increase of 32 percent over 1973. Net earnings were $9,261,000. On a fully diluted basis including extraordinary items, this amounted to $1.97 per share compared to the previous record of $.91 set in 1973. During 1974, all operating divisions achieved increased earnings except the plants in London, Ontario and Australia.

In Canada, the construction market was strong for the first six months but demand for our manufactured products decreased during the latter half of the year. Rapidly accelerating costs, particularly for raw material, were not fully compensated for by increased selling prices for our manufactured products within the Plumbing and Industrial Group.

New products contributed to the improved operating results of the Engineered Products Group, but, again cost increases resulted in inadequate profit margins on some major projects. A significant improvement in earnings for our United States operation was attributed to a greater share of the market, particularly for those products that have been developed during the past three years. A more detailed review of the 1974 operations for the Plumbing and Industrial Group and the Engineered Products Group is on pages 4 and 6 respectively.

Some comments are appropriate with respect to inflation in Canada and other countries where we have operations. The rate of inflation during 1974 (based on consumer price indexes) varied from about 11% in Canada and the U.S.A. to over 16% in the United Kingdom. These high rates of inflation were reflected in increased inventories and accounts receivable and despite the record net earnings, our bank credit lines were fully utilized at times during the year. Inflation also caused an erosion of the capital employed in the Company. Therefore, net earnings must increase to maintain adequate working capital to provide funds for replacement of plant and equipment and for expansion to meet our growth objectives.

Uncertainty about Canada's economy, along with record-high mortgage interest rates, contributed to the decline in residential housing activity during the latter half of 1974. The housing market in 1975 will depend, to a considerable extent, on government programs as well as the performance of the Canadian economy in general. Any beneficial effects flowing from the reduction in the federal sales tax on building materials, along with the drop in mortgage rates and stable land values, may well be offset by rising construction costs. However, the need for housing is still acute and there is every indication that, with an economic upturn during the latter part of 1975, housing starts may hopefully reach the level of 180,000 to 190,000 compared with 222,000 in 1974. This level of housing activity could result in lower operating profits for the Plumbing and Industrial Group.

The orders on hand are at an all-time high for the world-wide markets of the Engineered Products Group. Major product developments in our line of vapor transfer systems have been completed and we expect to gain a large share of this growing market. We are also continuing our program of product development and improvement in the traditional areas of our range of fluid handling equipment. The long-term outlook for our business is encouraging and we are optimistic that the Group will maintain its recent record of profitable growth.

With deep regret, we record the deaths of J.H. Stevens on May 28 and C.H. Ivey on September 7, 1974. Between them, they had served Emco for over 110 years. Both men had a strong sense of commitment and responsibility, which extended to unselfish work on behalf of the community. We are indebted for the leadership and service they gave to Emco and shall treasure the memory of our association with them.

We are aware of our corporate responsibility to be good citizens, and the measurement of our contributions to worthy organizations is, of course, a reflection of our ability to remain in business on a profitable basis. We also encourage our people in the various Emco divisions to participate in projects that benefit the community.

The partnership created through the investment by Masco Corporation in our Company has been of significant benefit to the Emco organization. The advantages are not only through the experience of the three Masco directors that serve on our Board, but also through the closer contact of many of our management group with the Masco people in the development of new products and new management techniques.

Our financial results for 1974 are a reflection of the efforts and dedication of our employees around the world, and, on behalf of the Board of Directors, we extend to them our sincere thanks.

C. N. CHAPMAN
President

London, Canada April 15, 1975

Review of Operations
PLUMBING AND INDUSTRIAL GROUP

PLUMBING AND INDUSTRIAL GROUP

DIVISIONS

Emco Supply — regional offices, Montreal, Toronto, Calgary; Thirty-two branches across Canada distributing plumbing, heating and industrial piping supplies to mechanical contractors and industry.

Arnold's Cove	Ottawa
Barrie	Peterborough
Belleville	Prince George
Calgary	Quebec
Edmonton	Regina
Guelph	Saint John
Halifax	Saskatoon
Hull	Sault Ste. Marie
Kitchener	Sherbrooke
Lethbridge	St. Catharines
London	Sudbury
Medicine Hat	Terrace
Moncton	Toronto (Weston)
Montreal	Ville de Brossard
North Bay	Windsor
Oshawa	Winnipeg

General Manufacturing — London Factory, London, Canada — manufacturer of plumbing, heating and industrial piping products for sale to distributors.
— Emco Plastics Limited, Brampton, Ontario — manufacturer of plastic plumbing and piping components.

Canadian Clyde Tube Forgings Limited, Toronto, Canada — supplier of steel welding fittings for industry.
Branches — Montreal, Vancouver, Edmonton

R. S. MacLean, Vice-President

Housing starts in Canada declined by 17% in 1974 but completions increased to a record level of 257,200 units. Commercial construction, which has been the mainstay of the non-residential sector for the past three years, continued relatively strong while industrial construction showed significant growth in the first half of the year.

Reflecting this pattern, production and sales of the Plumbing and Industrial Group reached record levels. However, in December, our London factory operations experienced a slowdown due to the lower level of housing construction activity.

GENERAL MANUFACTURING DIVISION

The capital expenditure program launched in 1971 to improve manufacturing efficiency and expand capacity continued through 1974. At the London factory, the floor space of the plant was extended, departments were relocated in larger areas, new machines were added and modern work flow systems introduced.

These changes reinforce our determination to improve our position in the industry through expansion of product lines and changing technology to meet current requirements and open future opportunities in growing markets.

In the physical changes, special emphasis was placed on improved work environment and employee morale. The most recent investment reflecting this concern relates to smoke and dust control. The new system, now being installed, will benefit foundry employees as well as the surrounding community by drastically reducing smoke and dust in the furnace area and emissions into the atmosphere.

Capabilities of the plastics plant in Brampton were also increased with the addition of new high speed injection moulding and ultrasonic welding machines. An additional raw material silo was also built as part of the expansion program. Work is now in progress on a new tool room which will be completed this year.

Our design engineers provide vital support to the group's objectives. They are continually engaged in development work for new products as well as improving performance of existing products. The "Tingle-King" showerhead and two-piece bath spout introduced last year have been well received by our customers.

The new central warehouse, located in Brampton, went into operation in the spring of 1974. This has resulted in improved customer service.

A new factory warehouse will be opened in Montreal to supply the wholesale market in Quebec. This facility along with the warehouses in Vancouver and Calgary are serviced through our Central Warehouse in Brampton. The regionalized warehousing has improved the service for our manufactured products to our wholesale customers.

CANADIAN CLYDE TUBE FORGINGS

Canadian Clyde Tube Forgings Limited, a wholly-owned subsidiary in Toronto, experienced another year of growth.

Early this year, the floor area of the plant was extended by 23,500 square feet. This additional space in an adjacent facility became available when Emco-Wheaton Limited moved into a recently acquired building. National distribution is extended through branches in Edmonton, Montreal and Vancouver.

EMCO SUPPLY

One of the most important factors in determining the value of goods, apart from their actual manufacture is their distribution. This added value stems from assembling products from various sources at convenient locations, having them ready when needed, packaging them in convenient units, shipping them where required, and maintaining inventories to match volume and type of demand.

During 1974, Emco Supply made further inroads into the market. Pressing for deeper market penetration, with carefully planned improvements in customer service, we made major capital investments in expansion and modernization of our distribution network.

New warehouses were opened in Moncton, Sherbrooke, North Bay, Medicine Hat and Terrace, increasing the total number of supply outlets across Canada to 32. Existing operations in St. Catharines and Halifax were relocated in larger, modern facilities. Extensions were made to warehouses in Toronto, Regina, Prince George and Ville de Brossard. Land was acquired for future replacement of existing facilities.

OUR MOST IMPORTANT RESOURCE

The Plumbing and Industrial Group has established a solid foundation with great resources in all areas: technology, facilities, financial strength and, most important, people.

Our people — men and women in manufacturing, engineering, sales, marketing, administration, accounting, personnel and other services — have a proven track record of achievement. We shall continue to build on their strengths for a mutually rewarding future.

In this spirit of partnership, we are committed to providing them with a stimulating and expanding work environment. We shall continue to open opportunities for self-advancement through growth, on-job training and other educational programs.

OUTLOOK

The short term outlook is, at best, one of cautious optimism as we face a slower growth rate. The residential sector will be soft in 1975, although reduced interest rates, lower federal taxes on building materials, other federal initiatives and provincial actions may stimulate the housing market. However, scarcity of serviced land and inflation will restrain the growth of the housing market. Commercial and engineering construction appear to be the source of real strength through 1975.

Review of Operations
ENGINEERED PRODUCTS GROUP

ENGINEERED PRODUCTS GROUP

DIVISIONS

Research and Development Centre – Margate, England

Wheaton Australia Pty. Limited – Sydney, Australia

Emco Wheaton Industria E Commercio S.A. (77% owned) Rio de Janeiro, Brazil

Emco Wheaton U.K. Limited – Margate, England

Emco Wheaton S.A. – Paris, France

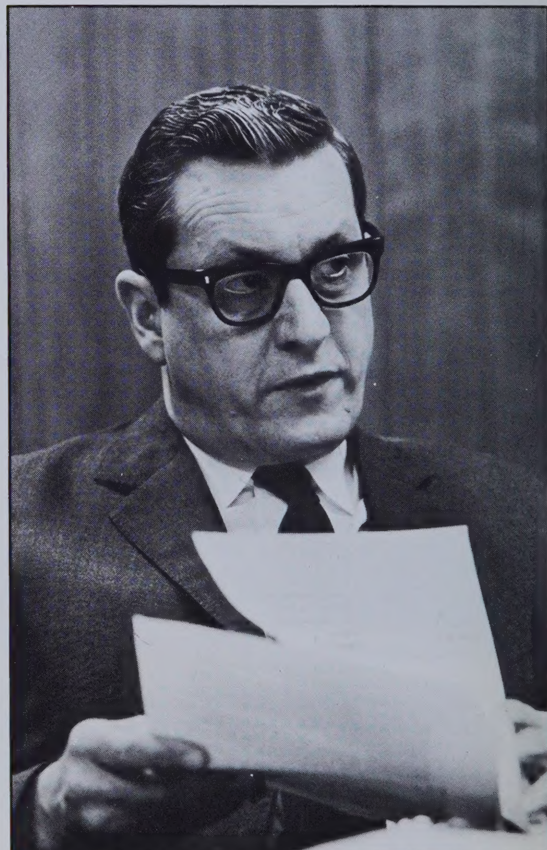
Emco Wheaton GmbH (76% owned) – Kirchhain, West Germany

Emco Wheaton Inc. – Conneaut, Ohio, United States

Emco Wheaton (Japan), Limited – Yokohama, Japan

Emco-Wheaton Limited – Toronto, Canada;
Branches –
Montreal, Calgary, Vancouver (Burnaby)

The Engineered Products Group manufactures and distributes engineered fluid handling equipment and systems used in the oil and petrochemical industries. These products, which are sold under the name, Emco Wheaton, include: service station equipment, marine loading assemblies, storage tank equipment, swing joints, loaders and unloaders, tank truck equipment, hose end couplings, dry breaks and fleet refueling systems.



J. G. Beresford, Vice-President

Despite worldwide economic uncertainties, group sales increased by almost 25%. While inflation accounted for some of this increase, significant contributions were made by the continuing expansion of our marine arm business and by products and systems designed for the U.S. market to meet federal emission control standards.

New product development is an important element in the group's growth. Our Research and Development Centre in England, along with divisional design personnel, continually review, test and develop new products. These activities are coordinated by our engineering staff located in the executive offices in Canada.

Our first order was received for the new marine arm bunkering unit which is used for fueling container ships, bulk carriers and super tankers. Mounted on a barge, it transfers bunker fuel from the barge to the ship. Designed by our Research and Development Centre, the marine arm bunkering unit is now offered from our division in Germany. The first unit will be installed in Antwerp, Belgium.

Significant progress has been made in the development of a vapor recovery nozzle, the latest item in our vapor transfer system. The vapor transfer system, as the term implies, contains and transfers vapors which otherwise would be lost to the atmosphere when gasoline is transferred from tank trucks to underground storage tanks at service stations and again in the transfer of gasoline from these tanks to the automobile. Our product engineering and marketing efforts in this respect are currently concentrated in the United States where emission control regulations continue to be introduced. However, all countries around the world are concerned with pollution abatement and our knowledge and experience gained in the U.S. market will be of great advantage in other areas adopting similar regulations.

CANADA

The Canadian division had a satisfactory year and, through an expansion of the sales organization, it continued to penetrate and extend its markets. The growth of this division has necessitated a plant expansion and, in February 1975, the Toronto operations were relocated in larger facilities. This move will permit future expansion of the division's activities.

U.S.A.

Considering the disruption earlier in the year due to a strike by the division's factory employees, the operating performance of Emco Wheaton Inc., showed considerable improvement and a satisfactory profit. At this time, there is a good order backlog and increased sales and profits are expected for 1975.

UNITED KINGDOM

Despite severe inflation and the poor state of the U.K. economy, operating results were very satisfactory. Export sales for this division were strong and account for approximately 50% of the total shipments. A number of large marine loader orders were completed during the last quarter. This division also has an excellent order book at this time.

GERMANY

Sales and operating profits increased over 1973. The high value of the Deutschmark in relation to other currencies has seriously affected the opportunities for export sales, but prospects for 1975 are good.

FRANCE

The effect of the energy crisis on our business in France has necessitated a redirection of our marketing activities. A major effort is being made to increase sales of existing and new products to industrial markets.

AUSTRALIA

The 1974 operating results for this division were very disappointing. Efforts are continuing to increase export sales and to increase the number of products that we manufacture for this market.

JAPAN

While operating results were again very satisfactory for 1974, it is expected that there will be reduced spending by the oil companies within Japan and greater efforts will be made to increase export sales in 1975.

BRAZIL

Our partnership in Brazil showed satisfactory results in its first full year of operation. Manufacturing activities have commenced and the prospects for 1975 look very promising.

OUTLOOK

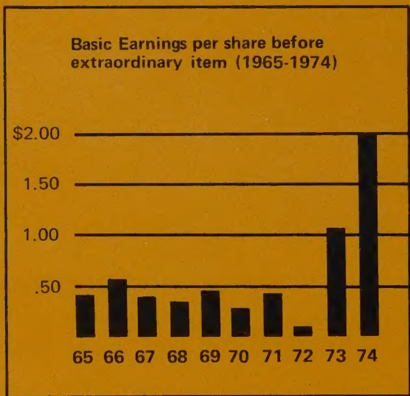
The outlook for continued growth in export is encouraging although currency revaluations, disparate rates of inflation and other monetary and fiscal variables create some uncertainties. All operating divisions have primary export markets and their combined exports represented 20% of the group's 1974 sales. Exports are made through distributors/agents whose activities are supported by five marketing coordinators who cover virtually every industrial market in the world.

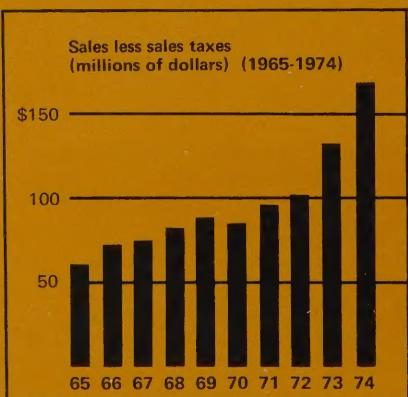
The needs of our principal customers, the oil companies, are continually changing due to new facilities, modernization of existing facilities and new safety and environmental regulations. Expectation of our continued growth is based upon a plan for increased penetration of our existing markets and the development of new products.

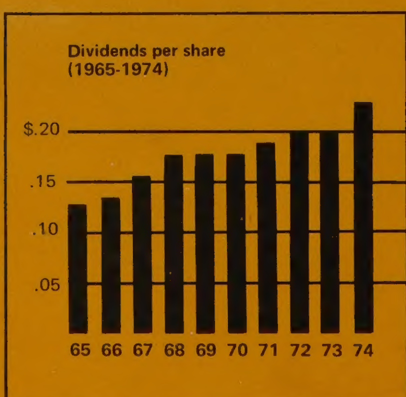
We believe that our people are capable of meeting the challenge of these changing needs. Through their able management and our technological strengths, we are determined to maintain and improve our reputation as a manufacturer and supplier of quality products to the oil equipment and petrochemical industries.

TEN YEAR FINANCIAL SUMMARY

Emco Limited and Subsidiaries







SALES, LESS SALES TAXES . . . .

CHANGES IN FINANCIAL POSITION

Funds provided:
- Funds provided from operations . . . .
- Increase in long-term debt . . . .
- Issue of common shares:
  - For cash . . . .
  - On conversion of 7% debentures . . . .
- Proceeds on disposal of property and plant . . . . .
  - Total funds provided . . . .

Funds used:
- Property, plant and equipment . . . .
- Reduction in long-term debt
  - 7% debentures . . . .
  - Other . . . .
- Redemption of second preference shares . . . .
- Dividends on second preference shares. . . . .
- Dividends on common shares . . . .
- Excess of purchase price of subsidiary companies acquired during the year over value of underlying net tangible assets . . . . . .
- Other . . . .
  - Total funds used . . . .

Increase (decrease) in working capital . . . .

Working capital at December 31. . . . .

COMMON SHARE RESULTS

Basic earnings:
- Before extraordinary item . . . .
- Including extraordinary item . . . .

Fully diluted earnings:
- Before extraordinary item . . . .
- Including extraordinary item . . . .

Book value at December 31 . . . .

Dividends paid . . . .

Return on shareholders' equity at January 1 (based on earnings before extraordinary item) . . . . .

NOTES —Amounts shown above are thousands of dollars results. Common share results reflect the 3 for effective May, 1965.

—In 1974, basic earnings per share and return on sha convertible debentures converted into common sha

1974	1973	1972	1971	1970	1969	1968	1967	1966	1965
72,550	130,329	100,542	95,926	83,810	89,380	83,399	74,325	72,331	60,692
10,310	5,032	1,673	2,774	2,267	4,439	2,509	2,513	2,727	2,408
—	280	—	6,000	5,000	—	—	3,867	—	6,561
—	—	—	41	91	2	33	88	87	29
4,890	—	34	—	—	—	—	—	—	—
152	1,049	427	—	24	60	169	—	294	287
15,352	6,361	2,134	8,815	7,382	4,501	2,711	6,468	3,108	9,285
3,054	2,984	2,594	1,791	939	1,768	1,928	2,402	2,006	778
5,776	—	34	—	—	—	—	—	—	—
555	81	123	1,543	3,605	638	258	948	561	184
—	—	—	—	442	239	297	357	298	234
—	—	—	—	7	17	25	35	45	53
998	756	756	723	689	687	686	623	554	488
—	75	214	—	—	—	—	1,115	—	—
(254)	(138)	17	201	231	26	(37)	466	(57)	(497)
10,129	3,758	3,738	4,258	5,913	3,375	3,157	5,946	3,407	1,240
5,223	2,603	(1,604)	4,557	1,469	1,126	(446)	522	(299)	8,045
31,404	26,181	23,578	25,182	20,625	19,156	18,030	18,476	17,954	18,253
2.00	1.07	.14	.45	.33	.47	.39	.43	.53	.46
2.08	1.12	.17	.45	.33	.91	.39	.45	.58	.49
1.91	.87	.14	.43	.33	.47	.39	.43	.53	.46
1.97	.91	.17	.43	.33	.91	.39	.45	.58	.49
8.02	6.10	5.20	5.27	5.02	4.88	4.15	3.88	3.91	3.50
.23	.20	.20	.18 3/4	.18 1/3	.18 1/3	.18	.16 1/4	.14 1/2	.13
32.0	20.5	2.7	8.9	6.7	11.3	10.0	11.0	15.1	14.6

eption of data under the heading Common share
effective July, 1971 and the 2 for 1 subdivision

uity are calculated on the assumption that the 7%
e year were converted on January 1, 1974.

Financial Statements

J. W. Adams, F.C.A., Executive Vice-President & Treasurer

FINANCIAL HIGHLIGHTS

Highlights of the 1974 financial statements are:

- Working capital increased from $26.2 million to $31.4 million at year-end.
- Trade receivables at $23 million show an improvement when related to annual sales. Bad debt expenses were .5% of sales during 1974, and full provision has been made for doubtful accounts.
- Inventories of $51.1 million contain $40.4 million of finished goods.
- Long term debt at December 31, 1974, was $10.1 million, and the debt to equity ratio was one to 3.6.
- Shareholders' equity increased from $23 million to $36.2 million as the result of the issue of 731,508 common shares on the conversion of $5,046,000 principal amount of 7% sinking fund debentures, and the reinvestment of a substantial portion of 1974 earnings. Book value per common share at year-end was $8.02.

Emco Limited and Subsidiaries

CONSOLIDATED BALANCE SHEET

December 31, 1974
with comparative figures for 1973

ASSETS	1974	1973
Current assets:		
Cash	$ 178,822	233,525
Marketable securities, at cost (quoted value $147,995; 1973, $147,390)	141,833	141,833
Trade accounts receivable, less allowance for doubtful accounts ($1,546,701; 1973, $946,807)	23,535,858	21,290,974
Inventories at the lower of cost or net realizable value	51,089,245	33,338,784
Prepaid expenses	714,666	514,308
Total current assets	75,660,424	55,519,424
Long-term receivables	100,547	180,479
Investment in partially owned company, at equity (note 1)	247,000	198,000
Property, plant and equipment, at cost less depreciation (note 2)	14,617,003	13,001,211
Unamortized debt discount and expense (note 3)	193,052	435,695
Deferred income taxes	108,294	—
	$90,926,320	69,334,809

LIABILITIES	1974	1973
Current liabilities:		
Bank indebtedness	$16,086,072	13,109,922
Notes payable	5,151,876	—
Accounts payable and accrued expenses	15,142,018	11,695,134
Dividends payable	270,835	189,120
Current portion of long-term debt	301,633	56,760
Income and other taxes payable	7,303,845	4,287,682
Total current liabilities	44,256,279	29,338,618
Deferred:		
Exchange translation gains (note 1)	203,474	202,815
Income taxes	—	173,706
	203,474	376,521
Long-term debt (note 3)	10,100,237	16,431,731
Minority interest in subsidiary companies	143,591	118,774
Shareholders' equity:		
Capital stock, common shares (note 4)	5,464,620	574,120
Retained earnings	30,758,119	22,495,045
Total shareholders' equity	36,222,739	23,069,165
	$90,926,320	69,334,809

See accompanying notes to consolidated financial statements.

On behalf of the Board:

C.N. CHAPMAN, Director **J.W. ADAMS,** Director

Emco Limited and Subsidiaries

CONSOLIDATED STATEMENT OF EARNINGS

Year ended December 31, 1974
with comparative figures for 1973

	1974	1973
Sales, less sales taxes:		
Plumbing and industrial group	$148,724,659	111,202,549
Engineered products group	23,824,876	19,126,494
	$172,549,535	130,329,043
Operating profit after minority shareholders' interest but before the undernoted items	$ 23,090,539	11,523,126
Investment income	9,938	10,703
Equity in earnings of partially owned company (note 1)	49,000	39,000
	23,149,477	11,572,829
Deduct:		
Depreciation	1,393,527	1,231,614
Interest on bank and other short-term advances	2,245,662	941,048
Interest on long-term debt	1,074,751	1,232,519
	4,713,940	3,405,181
Earnings before taxes on income	18,435,537	8,167,648
Taxes on income (note 6):		
Current	9,820,000	3,920,000
Deferred	(324,000)	224,000
	9,496,000	4,144,000
Earnings before extraordinary items	8,939,537	4,023,648
Extraordinary items	321,000	201,415
Net earnings	$ 9,260,537	4,225,063
Earnings per common share (note 5):		
Basic:		
Before extraordinary items	$ 2.00	1.07
Extraordinary items	.08	.05
Including extraordinary items	$ 2.08	1.12
Fully diluted:		
Before extraordinary items	$ 1.91	.87
Extraordinary items	.06	.04
Including extraordinary items	$ 1.97	.91

See accompanying notes to consolidated financial statements.

Emco Limited and Subsidiaries

CONSOLIDATED STATEMENT OF RETAINED EARNINGS

Year ended December 31, 1974
with comparative figures for 1973

	1974	1973
Amount at beginning of year	$22,495,045	19,101,048
Add net earnings	9,260,537	4,225,063
	31,755,582	23,326,111
Deduct:		
Dividends on common shares	997,463	756,481
Excess of purchase price of business acquired during the year over values ascribed to the underlying net tangible assets	—	74,585
	997,463	831,066
Amount at end of year	$30,758,119	22,495,045

See accompanying notes to consolidated financial statements.

AUDITORS' REPORT TO SHAREHOLDERS

We have examined the consolidated balance sheet of Emco Limited and subsidiaries as of December 31, 1974 and the consolidated statements of earnings, retained earnings and changes in financial position for the year then ended. Our examination included a general review of the accounting procedures and such tests of accounting records and other supporting evidence as we considered necessary in the circumstances.

In our opinion, these financial statements present fairly the consolidated financial position of the company and subsidiaries at December 31, 1974 and the consolidated results of operations and changes in financial position for the year then ended, in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

London, Ontario
February 18, 1975

PEAT, MARWICK, MITCHELL & CO.
Chartered Accountants

Emco Limited and Subsidiaries

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

Year ended December 31, 1974
with comparative figures for 1973

	1974	1973
Funds provided:		
Funds provided from operations	$10,310,207	5,032,370
Issue of common shares on conversion of 7% debentures	4,890,500	—
Assumption of mortgage	—	279,708
Proceeds on disposal of property and plant	151,550	1,048,807
Other	302,908	243,709
Total funds provided	15,655,165	6,604,594
Funds used:		
Property, plant and equipment	3,053,869	2,984,250
Reduction in long-term debt:		
7% debentures	5,776,000	—
Other	555,494	81,192
Dividends on common shares	997,463	756,481
Other	49,000	179,407
Total funds used	10,431,826	4,001,330
Increase in working capital	$ 5,223,339	2,603,264
Working capital at end of year	$31,404,145	26,180,806

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1974

1. **Principles of consolidation and basis of presentation:**
The accompanying financial statements consolidate the accounts of all subsidiary companies and all material inter-company balances and transactions have been eliminated.

The accounts of the subsidiary companies located outside Canada have been translated to Canadian dollars as follows: current assets, current liabilities and long-term debt — at rates current at the year end; fixed assets — at rates current on dates of acquisition; accumulated depreciation and related provisions against income — on the basis of dollar value of related assets; and operating income and other expenses — at average rates for the year. Gains resulting from such translation practices are deferred and losses in excess of previously deferred gains, accounted for by country, are charged to earnings. There were no significant translation losses charged to earnings in 1974.

The investment in the shares of the partially owned company (50 percent owned) is carried at cost adjusted by the company's share of its earnings since acquisition.

The investment in net assets at December 31, 1974 was geographically distributed approximately as follows:

Canada and United States	$30,775,000
Europe	3,889,000
Japan and Australia	1,170,000
Brazil	389,000

2. Property, plant and equipment:

	1974	1973
Buildings and roadways	$12,678,055	11,348,225
Machinery and equipment	12,521,749	11,271,505
	25,199,804	22,619,730
Less accumulated depreciation	12,611,040	11,539,548
	12,588,764	11,080,182
Land	2,028,239	1,921,029
	$14,617,003	13,001,211

Depreciation is generally provided on a straight line basis over the estimated useful lives of the assets. Depreciation rates are as follows: buildings 2.5% and 5%; roadways 10%; machinery and equipment 10% and 20%.

3. Long-term debt:

	1974	1973
Emco Limited:		
5 3/4% sinking fund debentures, due June 15, 1985	$ 4,592,000	4,867,000
9 3/4% sinking fund debentures, due July 15, 1990	4,987,000	5,000,000
7% convertible sinking fund debentures, due August 1, 1991	189,000	5,965,000
8% mortgage due September 1, 1975	279,708	279,708
United States subsidiary:		
6% mortgage note payable in monthly instalments of principal and interest of $3,585 U.S., due August 1, 1980 (U.S. $357,631)	354,162	376,783
	10,401,870	16,488,491
Less amounts due within one year included with current liabilities	301,633	56,760
	$10,100,237	16,431,731

During the year $5,046,000 principal amount of 7% convertible sinking fund debentures were converted into 731,508 common shares and $730,000 principal amount were repurchased for cancellation.

Long-term debt falling due or to be met out of sinking fund payments in the five years ending December 31, 1979, after taking into account the principal amount of debentures repurchased by the company which have been tendered to the trustee in respect of future sinking fund payments, aggregates $301,633 in 1975; $326,000 in 1976; $413,000 in 1977; $436,000 in 1978 and $453,000 in 1979.

The unamortized debt discount and expense relating to the 9 3/4% sinking fund debentures is being amortized over the term of the debentures using a sum of the digits method.

4. Capital stock:

(a) Authorized, issued and outstanding:

	Number of Shares		
		Issued and Outstanding	
	Authorized	**1974**	**1973**
First preference shares with a par value of $100 each	150,000	–	–
3% cumulative redeemable second preference shares with a par value of $10 each	61,600	–	–
Common shares without nominal or par value	12,000,000	4,513,913	3,782,405

The value assigned to the 731,508 common shares issued in 1974 on conversion of debentures ($4,890,500) was after deduction of the related debenture discount, net of income taxes applicable thereto.

(b) Share options:
At December 31, 1974, 185,025 common shares had been reserved for issuance under share option plans for certain key executives. Options on 14,925 common shares were outstanding at prices ranging from $4.79 to $5.066, the last of which expires in 1977.

(c) Share purchase plan:
During 1968, a share purchase plan was approved whereby the employees of the company and its subsidiaries (excluding officers and directors of Emco Limited) may purchase common shares of the company. As at December 31, 1974, there were 128,145 shares available for future subscriptions. There were no transactions during 1974.

(d) Dividend restrictions:
The trust deeds relating to the debentures each contain provisions whereby dividends may not be declared or paid, other than stock dividends, and the company may not effect any reduction to its capital stock which would reduce net current assets and shareholders' equity (as therein defined) below certain levels. At December 31, 1974 the net current assets and shareholders' equity (as so defined) were substantially in excess of minimum levels.

(e) Conversion privilege:
The 7% convertible sinking fund debentures are convertible into common shares without par value in the capital of the company at any time prior to the close of business on August 1, 1977, on the basis of 127 common shares for each $1,000 principal amount of debentures; and thereafter and at any time prior to the close of business on August 1, 1980, on the basis of 112 common shares for each $1,000 principal amount of debentures.

For debentures converted into common shares prior to the close of business on August 1, 1974, common share purchase warrants were issued on the basis of 50 warrants for each $1,000 principal amount of debentures so converted entitling the holder of such warrants to purchase one new common share for each warrant held at a price of $7.87 per share, at any time prior to the close of business on August 1, 1977, and thereafter and at any time prior to the close of business on August 1, 1980 at a price of $8.93 per share. To December 31, 1974, 253,600 warrants had been issued and were outstanding at that date.

The company has covenanted to reserve a sufficient number of common shares to be available for conversion of the 7% debentures and for issue upon exercise of the common share purchase warrants.

5. **Earnings per share:**
Earnings per share are calculated using the weighted daily average number of shares outstanding.

Basic earnings per share in 1974 have been adjusted to reflect the assumption that the 7% convertible sinking fund debentures converted into common shares during the year were converted at the beginning of the year and the related interest net of income tax eliminated. Otherwise the basic earnings per share would have been $2.18 before extraordinary items and $2.26 including extraordinary items.

Fully diluted earnings per share are calculated on the assumption that all options, warrants, conversion privileges and related rights to warrants outstanding at the end of the year were exercised at the beginning of the year; and that funds derived therefrom had been used to reduce bank indebtedness and related interest costs. The interest deducted less related income taxes was $110,751 (1973 – $96,162).

6. **Taxes on income:**
Certain subsidiaries suffered operating losses during the year and such losses did not result in any current recovery of income taxes. The potential income tax benefits associated with such operating losses and with the operating losses of certain subsidiaries in prior years are not recognized in the accounts. These operating losses, which aggregate approximately $1,454,000 are available to reduce taxable income which might otherwise be reported in certain future years. The availability of these losses for that purpose expires as to $902,000 in 1977, $83,000 in 1978, $260,000 in 1979, $15,000 in 1980 and $194,000 in 1981.

7. **Directors and senior officers remuneration:**
The aggregate direct remuneration paid or payable by the company to directors and senior officers was $723,000 for the year ended December 31, 1974 (1973 – $680,000).

8. **Pension costs:**
The company has no significant liability for past services under its pension plans.

Emco Limited
Box 5300, London, Canada N6A 4N7
Subsidiaries in Australia, Brazil, Canada, France, Great Britain, Japan, the United States and West Germany

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